

Why Companies will have difficulties claiming Business Interruption Insurance for Covid-19 Losses



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Individual Highlights:

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Way Forward

WHAT IS BUSINESS INTERRUPTION INSURANCE?

Business interruption insurance (also known as business income insurance) is a type of insurance that covers the loss of income that a business suffers after some physical loss or damage due to covered events. This type of insurance also covers operating expenses, a move to a temporary location if necessary, payroll, taxes, and loan payments. The income loss covered may be due to an event related closing of the business facility or due to the rebuilding process after an event.

It differs from property insurance in that a property insurance policy only covers the physical damage to the business, while the additional coverage allotted by the business interruption policy covers the profits that would have been earned. This extra policy provision is applicable to all types of businesses, as it is designed to put a business in the same financial position it would have been in if no loss had occurred.

This type of coverage can be added onto the business' property insurance policy or comprehensive package policy such as a business owner's policy (BOP) or as part of a standalone policy in some jurisdictions. In India, it is sold as a standalone cover and also as a package policy or add-on cover. Since business interruption is included as part of the business' primary policy, it only pays out if the cause of the loss is covered by the overarching policy or a defined event in the case of a standalone.

Coverage Options in a Business Interruption Insurance

The following are typically covered under a business interruption insurance policy:

 **Profits** - Profits that would have been earned (based on prior months' financial statements).

 **Fixed costs** - Operating expenses and other costs still being incurred by the property (based on historical costs).

 **Temporary location** - Some policies cover the extra expenses for moving to, and operating from, a temporary location.

 **Commission and training cost** - Business Interruption (BI) policy essentially covers the cost of providing training to the operators of the machinery replaced by the insurer following the insured events.

 **Extra expenses** - Reimbursement for reasonable expenses (beyond the fixed costs) that allow the business to continue operation while the property is being repaired.

This coverage extends until the end of the business interruption period determined by the insurance policy. Most insurance policies define this period as starting on the date of the covered peril and the damaged property is physically repaired and returned to operations under the same condition that existed prior to the disaster.



DIFFICULTIES FACED AMID COVID-19

India's lockdown to contain the spread of Covid-19 has brought the nation and businesses to a halt, causing losses. While businesses with the capability to work remotely/from home are doing so, a large chunk of the business are still not operational. Most big companies do have disaster/business continuity planning and do buy a Business Interruption Cover from Insurance Companies, but according to many insurers, such policies do not cover a pandemic like Covid-19.

The hospitality and travel sectors are amongst the worst affected, in spite of a host of measures taken by the government to boost liquidity, provide moratorium on loans and ease compliance. Whilst these measures help to an extent, it cannot recover the losses faced. Thereby, market leaders are wanting the Government/Insurance Regulatory and Development Authority of India (IRDAI) to help ensure that loss of profit in business due to Covid-19 is covered in the standard Business interruption Cover purchased.

In fact in possibly the first of its kind, a lawsuit has been filed by a restaurant chain on 16 March 2020 in the State of Louisiana, USA, in relation to coverage under a specific type of Business interruption Policy. Although the case has a lot of very specific circumstances, it does highlight the type of issues that business will face¹.

On the flip side it is seen that Business interruption Cover is not very widely sold in India as they are less prevalent among small and medium enterprises. Much more popular are the basic fire policies covering property damage perils like fire and catastrophic or Acts of God perils like flood and earthquake. Also, traditionally if a claim is triggered on property damage, only then is business interruption cover triggered.

¹ <https://www.whiteandwilliams.com/resources-alerts-First-Coronavirus-Coverage-Suit-Filed-For-Business-Interruption.html>

Although the scope of business interruption coverage varies widely from policy to policy, common issues that are pertinent during the present crisis include the following:

If business ceases or diminishes because an individual infected with the coronavirus was on the company's premises, is the virus considered a direct physical loss needed to make a claim under a business interruption policy? The answer to this question in the context of the coronavirus will depend upon the terms of the policy, and it may also depend upon the jurisdiction in which the business operates. Some courts interpret the “direct physical loss” requirement broadly. For example, in a case², the court found that odours emitted from defective carpeting could constitute a physical injury sufficient to trigger coverage. And, in another, the court³ found that carbon monoxide contamination was a “direct physical loss.” There are, however, examples where courts have taken a narrower interpretation ruled⁴ that “intangible harms such as strong odours and the presence of mold and/or bacteria in the air and ventilation system” were not a “direct physical loss.” Or ruled⁵ “that mould on siding” did not constitute “property damage” sufficient to trigger coverage because it did not impair the “structural integrity of the house” and could be “cleaned from the siding.”

Is there a virus exclusion in the policy and how broad is the exclusion? Some policies expressly exclude coverage for virus and bacteria related claims. Even where there is no explicit exclusion for viruses or bacteria, this issue may also arise in the context of a pollution exclusion, which may exclude coverage for pollutants, irritants, and contaminants. In defining these terms, the policy may exclude viruses from the definition of a “contaminant.” It is to be noted that certain industries, like the hospitality, travel, and healthcare sectors, may have specific coverage for losses resulting from “communicable diseases,” including viruses.

Is there coverage for losses due to shutdowns imposed by civil ordinances or authorities, such as orders preventing businesses from opening to the public or preventing employees, customers, and others from entering the premises? If an order from a civil or military authority prevents access to company property, resulting in the impairment of operations, there may be business interruption coverage for such losses. This assumes there is no policy exclusion for losses due to virus outbreaks.

Is there coverage because access to your business is prohibited due to physical damage to property (yours or someone else's)? Relatedly, there may be coverage where a business cannot be accessed, or access is limited, because of damage to the property. This raises the question, noted above, whether the presence of concern over viral contamination is deemed to be physical damage to property. Also, insurers believe that business interruption losses arising out of shutdown due to the pandemic cannot be reimbursed as no contributions have been made by way of premium for paying such a loss.

Do you have “contingent” business interruption coverage due to the loss of a key supplier? If your company depends upon the timely receipt of products from key suppliers, you may have business interruption coverage if the operations of that supplier are disrupted. Likewise, other supply-chain disruptions, such as interruptions in the delivery of food or supplies to a hotel, may be covered under business interruption policies. One would need to clarify whether the coverage only includes the circumstance when the supplier disruption is due to explicit physical damage of the supplier's property or something broader.

Do you have “leader” property coverage, meaning coverage for losses resulting from damage to an important nearby property (such as a mall or amusement park)? If another business is affected, and that business provides substantial business to your company, you may have business interruption coverage for those losses. But, again, this type of coverage may be subject to policy exclusions for virus outbreaks.

² Essex Insurance Co. v. BloomSouth Flooring Corp., 562 F.3d 399 (1st Cir. 2009)

³ Matzner v. Seaco Ins. Co., 1998 Mass. Super LEXIS 407 (Mass Super Ct. 1998)

⁴ Universal Image Productions, Inc. v. Chubb Corp., 703 F. Supp. 2d 705 (E.D. Mich. 2010)

⁵ Mastellone v. Lightning Rod Mut. Ins. Co., 884 N.E.2d 1130 (Ohio Ct. App. 2008)

In addition to these questions, which are key to determining whether your company has business interruption coverage for coronavirus-related losses, best practices when submitting a business interruption claim need to be adopted. Actuarial or Insurance Consultants/Brokers should be able to assist you with the same.

Alas, there is simply no blanket answer as to whether Business Interruption policies cover claims resulting from the unprecedented circumstances flowing from Covid-19. The terms of the policy will control claims, along with the applicable law.

To determine whether your company has coverage for such claims, look at your policies and consult with your broker and legal counsel. K. A. Pandit Consultants and Actuaries', Enterprise Risk Management team would be available to help design such covers or consult for any good practices for claims to be filed or simply answer any questions you may have.

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